

Memorandum

To: Mr. John Gibbs
Out-of-State Sacramento
District Office - OH

Date: October 18, 1993

From: Thomas Cooke, Tax Counsel
Legal Division - MIC:82

Subject: **LIMITED LIABILITY COMPANIES**

The Legal Division has received your memorandum dated August 18, 1993 in which you state that some states have authorized a form of company ownership called limited liability companies. You also state that at least four states have created this type of entity and you ask if the Board should treat these entities as corporations or limited partnerships.

The following statement appears in Commercial Clearance House, State Tax Reporter, Texas, § 5-013:

"Effective August 26, 1991, Texas authorizes the creation of limited liability companies. A limited liability company is a business entity that shares characteristics of both partnerships and corporations. Like a partnership, a limited liability company is a pass-through entity in which the profits and losses are passed through to its members. However, unlike a limited partnership in which the individual partners are personally liable for amounts up to and including the amount of their contributions to the partnership or a general partnership in which all members are liable for the partnership obligations, members of a limited liability company incur no personal liability. The characteristics of a limited liability company are also similar to those of a 'S' corporation, but limited liability companies are not subject to the many restrictions placed on 'S' corporations, such as the limitations on the number and types of shareholders, the allowable classes of stock, and the flow-through of losses

"For federal purposes, for a limited liability company to be treated as a partnership it must have more partnership characteristics than corporate characteristics. Under federal Regulation 301.7701-2, an association may avoid classification as 'an association taxable as a corporation' if it lacks at least two of

the following four corporate characteristics: (1) continuity of life, (2) centralization of management, (3) limited liability, and (4) free transferability of interests. In Rev. Rul. 88-76, the IRS classified a Wyoming limited liability company as a partnership for federal income tax purposes. The IRS has also issued letter rulings determining that specific limited liability companies organized in Florida (Ltr. Ruls. 8937010 and 9010027) and Utah (Ltr. Rul. 9219022) will also be treated as partnerships for federal income tax purposes even if they are treated as corporations by the state in which they are organized."

Among the states which permit the formation of limited liability companies are Colorado, Florida, Kansas, Nevada, Texas, Utah, Virginia and Wyoming.

California has not recognized, or regulated, the concept of a limited liability company. A bill to permit the formation of limited liability companies in California was introduced in the California Legislature but was not passed.

A limited liability company formed under the laws of another state is a "person" within the meaning of Revenue and Taxation Code section 6005 and will be responsible for California Sales and Use Tax and is required to register as a "seller". We recommend that any permit issued to a limited liability company clearly indicate that the entity is not a corporation. It is our recommendation that the Board's records note that the entity as "[name], a [State] limited liability company."

With respect to collections, we have been unable to discover any California legislation or case law which either permits or prohibits personal liability of a limited liability company's members for the debts of the entity. Revenue and Taxation Code section 6829 which, in some circumstances, imposes liability on corporate officers for the tax liability of a corporation is inapplicable to limited liability companies. Since California's Sales and Use Tax Law does not mention limited liability companies, in the absence of any direction from California courts or the Legislature, there is no authority to impose any tax liability accruing to a limited liability company on the company's members.

TJC:plh

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cc: Mr. Gary Jugum - MIC:82
Mr. James Speed - MIC:47
Mr. Glenn Bystrom - MIC:49
Ms. Sue Coty - MIC:46
Mr. Gordon Adelman - MIC:82